Office Supreme Court, U.S.
FILED
MAR 16 1970
JOHN F. DAVIS, CLERK

IN THE

Supreme Court of the United States

October Term, 1969

No. 1180

TODD SHIPYARDS CORPORATION,
Petitioner,

vs.

MASTAN COMPANY, INC., etc.,
Respondents.

BRIEF IN OPPOSITION TO PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

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Statement of the Case

At stake in this admiralty *in rem* action is the distribution of $55,085.37, deposited in the Registry of the District Court, following the foreclosure and sale of the SS Sapphire Sandy (hereinafter "Sandy") by the United States Marshal. The original sale proceeds secured by the United States Marshal were $160,000. This sum was reduced to $55,085.37 by payments for administrative costs and by payments in settlement of lien suits filed below by seamen for wages. After the latter reductions, there remained only two contestants to the fund of $55,085.37, to wit, the Peti-

tioner, Todd Shipyards Corporation (hereinafter "Todd") and the Respondent, Mastan Company Inc. (hereinafter "Mastan").

Mastan brought the suit below *in rem* against the Sandy, a vessel owned by Sapphire Steamship Company (hereinafter "Sapphire") to foreclose a mortgage thereon, which it claimed to be a preferred ship mortgage under the U. S. Ship Mortgage Act of 1920 (46 USC §911 et seq.). Other maritime lien claimants, such as Todd, also filed *in rem* suits below against the Sandy. The District Court appointed a Special Master, who determined that Mastan was entitled to the remaining fund in the District Court ($55,085.37) by reason of its being the holder of a valid first preferred ship mortgage on the Sandy within the purview of the U. S. Ship Mortgage Act.

Mastan's ship mortgage originally secured a total loan from Mastan to Sapphire in the amount of $1,296,000. The Special Master, the District Court and the Court of Appeals found that the sole purpose of this loan was to enable Sapphire to purchase three ships, one of which was the Sandy. The other ships were the SS Sapphire Gladys (hereinafter "Gladys") and the SS Sapphire Etta (hereinafter "Etta"). Thus, Mastan's mortgage was in effect a purchase money mortgage. This loan was made by Mastan in two parts, i.e., $864,000 on December 29, 1965 and $432,000 on January 21, 1966. The first loan installment was used to purchase the *Sandy* and *Gladys*. To secure said loan, Sapphire granted Mastan a First Preferred Fleet Ship Mortgage on the *Sandy* and *Gladys*. The second loan installment was used to purchase the *Etta*. To secure said loan, the First Preferred Ship Mortgage was

amended by a Supplemental Agreement in which the Mortgage on the *Sandy* and *Gladys* was extended to include said loan and a preferred ship mortgage granted on the *Etta* to cover the entire loan.

Thereafter and in August of 1966 Mastan, at Sapphire's request, extended the term of Sapphire's loan and reduced the monthly payments thereunder. For this Mastan charged a finance fee of $52,817.13 which was, in effect, loaned by Mastan to Sapphire, the said sum being added on to the then outstanding indebtedness due under the original loan of $1,296,000. To secure the latter, the aforesaid original First Preferred Fleet Ship Mortgage, as amended by the Supplemental Agreement, was further amended by a Supplemental Indenture which extended the mortgage on the *Sandy*, *Gladys* and *Etta* so as to cover the additional loan of $52,817.13.

The admiralty jurisdiction of the District Court was strictly *in rem* and was invoked to determine the validity and priority of competing maritime lien rights in the Sandy and the proceeds of her sale. There was no issue as to *in personam* rights of any of the lien contestants either between themselves or against Sapphire. It is conceded by Todd that the Ship Mortgage Act of 1920 is the controlling statute which governs the priority of the liens filed in the proceedings below. Such Act (46 USC §953) grants a ship mortgage, within its coverage, lien priority

> "over all claims against the vessel, except (1) preferred maritime liens and (2) expenses and fees allowed and costs taxed, by the court".

The Act (46 USC §953) defines a "preferred maritime lien" as either (A) "a lien arising *prior* in time *to the re-*

cording and endorsement of preferred mortgage'' or (B) ''a lien for damages arising out of tort, * * *'' (Emphasis supplied.)

It was found below and it is conceded by Todd that the First Preferred Fleet Ship Mortgage and the Supplemental Agreement thereto (which secured the original loan of $1,296,000) were duly recorded and endorsed on December 29, 1965 and January 21, 1966 respectively.[1] Todd concedes that its repairs were rendered after such recordation and endorsement.

By reason of the fact that Mastan's Original Mortgage and the Supplemental Agreement thereto were recorded and endorsed prior to the rendition of Todd's services, the Ship Mortgage Act gives the lien of Mastan's mortgage priority over the lien of Todd up to the amount outstanding on the original loan[2] unless such mortgage is invalid un-

1. The Ship Mortgage Act requires, as a condition precedent to preferred status that (a) the mortgagee be a U.S. citizen (46 USC §922), and (b) that the mortgage comply with the public notice provisions of such Act (46 USC §§921, 922). These provisions require that the mortgage, together with a good faith affidavit executed by the mortgagor, be recorded with the U.S. Coast Guard at the mortgaged vessel's port of documentation and further, require that certain information about the mortgage be endorsed on the mortgaged vessel's papers. The courts below found, and Todd does not contest, that Mastan's mortgage and all the amendments thereto complied with the just noted recording provisions and further that Mastan was a United States citizen.

2. As noted above, the mortgage documents securing the original loan to Sapphire of $1,296,000 (i.e., the Original Mortgage and the Supplemental Agreement thereto) were recorded and endorsed prior to any rendition of repairs by Todd. The evidence below showed that up to the time of its mortgage default, Sapphire had repaid Mastan the sum of $531,000.68, which means that there is still a principal debt of $715,068.32 due on the original loan to which the lower courts have held Mastan has lien priority. This amount is monumentally in excess of the fund in the Registry of the District Court ($55,085.37).

der the Ship Mortgage Act or unless Todd's lien be a "preferred maritime lien," as defined above, i.e. if its lien be deemed based on tort.

Realizing the above, Todd advanced below a dual attack on Mastan's lien priority i.e. (a) Mastan's mortgage was fraudulent and thus is not valid under the Ship Mortgage Act and (b) Todd's lien is a "preferred maritime lien" sounding in tort and is superior to that of Mastan's mortgage even if the latter is valid under the Ship Mortgage Act.

The Special Master, District Court and the Court of Appeals found that the mortgage transactions between Sapphire and Mastan were untainted with the slightest fraud. To obviate the patent lack of fraud, Todd sought below to graft upon the provisions of the Ship Mortgage Act concepts of presumed-in-law fraud found in the Debtor and Creditor Law of New York, i.e., concepts founded, in part, on a standard of insolvency or inadequacy of capital assets of a transferor at the time of a transfer. Likewise to support its characterization of tort lien, Todd relies on the concept of insolvency, i.e., that Sapphire was insolvent when it ordered the repairs and that this condition was fraudulently concealed from Todd by both Sapphire and Mastan.

In support of the above tack, Todd contended below and contends here, that the District Court found, and implies that the Special Master found, that Sapphire was insolvent at the time of the mortgage transactions to the knowledge of Mastan. In its petition, Todd supports this contention by quotations from the District Court's opinion.

Mastan submits that these quotations are extracted out of context and that there was a complete absence of a finding of insolvency and knowledge thereof below. Mastan, however, need not dwell upon this, as the courts below held that, even assuming insolvency of Sapphire at the time all the mortgage transactions to the knowledge of Mastan, Mastan's mortgage is valid under the Ship Mortgage Act of 1920 and is entitled to priority over the purported lien of Todd. Todd, however, goes beyond quotations of the District Court's opinion and launches into a lengthy review of the evidence below in an attempt to justify its contention of fraud, insolvency and knowledge thereof in Mastan. Mastan would be remiss if it did not place on the record the notation that this evidential review amounts to nothing more than a self-serving and blatant distortion of the evidence below. The merits of Todd's evidential incursion aside, Mastan submits that the same is improper as certiorari is not granted to review evidence or discuss specific facts. *U. S.* v. *Johnston*, 268 US 220, 227 (1925).

I

Reasons for Denial of the Writ

1. The decision below sustaining the validity of Mastan's mortgage and the priority of that mortgage over the purported lien of Todd does not present an important federal question as such decision was patently correct nor does there exist any conflict between that decision and the decision of any other court.

Todd's assault upon the finding of validity of Mastan's mortgage, rendered by the courts below, is founded upon

§922(a)(3) of the Ship Mortgage Act (46 USC §922(a)(3)). This section requires that an affidavit be filed with the mortgage

> "* * * to the effect that the mortgage is made in good faith and without any design to hinder, delay or defraud any existing or future creditor of the mortgagor or any lienor of the mortgaged vessel;"

Todd asserts that the Ship Mortgage Act requires more than the mere formality of the filing of a good faith affidavit; that the Act requires as a matter of substance that the mortgage be given in good faith and not as a device of the mortgagor or the mortgagee to perpetrate fraud. Mastan wholeheartedly agrees. Todd, however, goes beyond this truism and without favor of citation to either the legislative history of the Ship Mortgage Act or case authority contends that the Uniform Fraudulent Conveyance Act, or more specifically the New York version thereof (Debtor and Creditor Law), should have been used as a standard for fleshing out the meaning of §922(a)(3). Todd specifically points to §§276, 273 and 274 of the New York Debtor and Creditor Law.

As the point of nexus, Todd alludes to Section 276 of the Debtor and Creditor Law which reads, in part, as follows:

> "Every conveyance made and every obligation incurred with *actual intent, as distinguished from intent presumed in law*, to hinder, delay, or defraud either present or future creditors is fraudulent as to both present and future creditors." (Emphasis supplied)

The similarity between the above language and that of Section 922(a)(3), says Todd, makes such Section applicable to the Ship Mortgage Act. Such interpolation is not,

however, supported by citation of authority. From this base of similarity in language, Todd then skips to Sections 273 and 274 of the Debtor and Creditor Law, again without citation of any authority, and says these, too, are incorporated in Section 922(a)(3) of the Ship Mortgage Act. The latter two sections introduce the concepts of insolvency and inadequacy of capital assets of a transferor as elements to be considered in the concept of presumed in law fraud. Section 273 reads as follows:

> "Every conveyance made and every obligation incurred by a person who is or will be thereby rendered insolvent is fraudulent as to creditors without regard to his actual intent if the conveyance is made or the obligation is incurred without a fair consideration."

Section 274 reads as follows:

> "Every conveyance made without fair consideration when the person making it is engaged or is about to engage in a business or transaction for which the property remaining in his hands after the conveyance is an unreasonably small capital, is fraudulent as to creditors and as to other persons who become creditors during the continuance of such business or transaction without regard to his actual intent."

The concepts of insolvency and inadequacy of capital assets found in Sections 273 and 274 are obviously not elements of Section 276, for, if they were there would be no need to promulgate Sections 273 and 274. While Section 276 has language similar to that in Section 922(a)(3) of the Ship Mortgage Act, there is no analogy of language or concept between the latter and Sections 273 and 274 of the Debtor and Creditor Law. It is submitted that to read the dissimilar language and concepts of Sections 273 and 274 of the

Debtor and Creditor Law into the Ship Mortgage Act would amount to blatant perversion of statutory construction. Thus, Mastan submits that even if one grants that Section 922(a)(3) of the Ship Mortgage Act may take some benefit from the New York Debtor and Creditor Law, Sections 273 and 274 thereof cannot be a part of that benefit.

The language of Section 276 of the Debtor and Creditor Law expressly requires a finding of "actual" fraudulent intent, and expressly excludes fraudulent intent presumed in law. Thus, the standards of imputed intent found in Sections 273 and 274 (insolvency and inadequacy of the capital of the transferor), even if found to exist, would not work a violation of Section 276. Neither suspicion nor presumption, but only proof of fraudulent intent, *as a matter of fact*, spells out a violation of Section 276, *First Nat. Bank of Batavier* v. *Franke*, 1 AD 2d 539, 151 N.Y.S. 2d 596, aff. 3 NY 2d 849, 144 NE 2d 727; *Langford* v. *Fessenden*, 220 AD 258, 221 N.Y.S. 424; *Matter of Decker*, 149 Misc. 364, 268 N.Y.S. 280; *Shay* v. *Abdella*, 131 Misc. 175, 225 N.Y.S. 2d 517; *Lupia* v. *Lupia*, 190 N.Y.S. 2d 733. Nor can a violation of Section 276 be founded upon mere intent to hinder or delay creditors, actual fraudulent intent being absolutely necessary, *Doehler* v. *Real Estate Board of New York Bldg. Co.*, 150 Misc. 733, 270 N.Y.S. 386; *Irving Trust Co.* v. *Kaminsky*, 19 F. Supp. 816, 818 (S.D.N.Y. 1937); *Ruhl* v. *Phillips*, 48 NY 125 (1871). The Special Master, the District Court and the Court of Appeals found that Mastan's mortgage transactions were untainted with the slightest fraud. Thus, even if we deem that Section 276 of the Debtor and Creditor Law has some application, Todd would gain naught.

Further, it is to be noted that both Sections 273 and 274 of the Debtor and Creditor Law expressly require, as a condition precedent, to violation, that the complained of transfer be without "fair consideration". The case law has made it clear beyond peradventure that, even where there is insolvency at the time of transfer or even where a transfer leaves inadequate capital, a violation of Sections 273 and 274 cannot occur, if the transfer was given or made for "fair consideration" *Huit Corp. Siskind*, 30 Misc. 2d 598, 219 N.Y.S. 2d 982; *Dochlen* v. *Real Estate Board of New York Bldg. Co., supra*; *Kamisher* v. *Sinicropi*, 192 N.Y.S. 2d 240; *Kelly* v. *Farmers Production Credit Assn.*, 88 N.Y.S. 2d 872; *Meriam* v. *Wimpfheimer*, 25 F. Supp. 405 (S.D.N.Y. 1938). The Special Master, the District Court and the Court of Appeals found that Mastan's mortgage transactions were patently supported by fair and full consideration. Thus, §§273 and 274 of the Debtor and Creditor Law, even if deemed applicable, would gain Todd nothing.

In its petition, Todd relies heavily on the cases *In the Matter of Lea Fabrics, Inc.* and *Dean* v. *Davis*. *Lea Fabrics* concerned The New Jersey Corporation Act and the *Dean* case the Bankruptcy Act, both of which are far removed from the New York or even Uniform Fraudulent Conveyance Act, which Todd uses by analogy in its attempt to graft the concept of insolvency onto the Ship Mortgage Act.

The dictates of statutory construction and the finding of facts below aside, it is paramount to note that neither in §922 (a) (3) nor anywhere else does the Ship Mortgage Act stipulate that insolvency of the mortgagor or the status

of his capital assets at the time of a mortgage transaction is an element by which the good faith of the transaction is to be judged. If the latter were elements of concern, it is submitted the Ship Mortgage Act certainly would have said so, as does the Debtor and Creditor Law (§§273, 274).

Mastan submits that the Court of Appeals was patently correct in ruling that the submission of the Ship Mortgage Act to the idiosyncrasies of various state standards could not be sanctioned, as same would run afoul of the requirement that federal ship mortgages have a uniform and a harmonious application throughout the land and in the international sphere, a requirement dictated by both the Constitution and the Ship Mortgage Act, itself. *Panama R.R. Co.* v. *Johnson*, 264 U. S. 375 (1924); *Pope & Talbot, Inc.* v. *Hawn*, 346 U. S. 406 (1953); *U. S.* v. *Oil Screw Ken Jr.*, 275 F. Supp. 792 (E.D. La. 1967); *Walter E. Heller & Co.* v. *The M/V Mr. Ed*, 270 F. Supp. 830 (E.D. La. 1967); *U. S.* v. *American Gas Screw Franz Joseph*, 210 F. Supp. 581 (D. Alaska 1962).

The federal cases which have interpreted §922 (a) (3) of the Ship Mortgage Act have made it clear the type of mortgage transaction which would run afoul of that section is one founded upon actual fraudulent intent (i.e. the typical example being a sham mortgage given to a dummy not founded upon any consideration). *Pascagoula Dock Station* v. *Merchants & Marine Bank*, 271 F. 2d 53 (5th Cir. 1959); *Flood* v. *American Oil Screw Trawler, Francis McPherson*, 258 F. Supp. 768 (E.D. Mass. 1966); *The R. Lenahan*, 10 F. Supp. 497 (E.D. Pa. 1935). None of the federal cases which have dealt with the requirement of good

faith of a preferred ship mortgage have implied, much less found, that the financial status of the mortgagor, be it insolvency or inadequate capital, is a pertinent inquiry. Indeed, the one case where the topic of the mortgagor's financial status was mentioned, shows just the opposite. In *Pascagoula Dock Station* v. *Merchants & Marine Bank*, *supra*, a lien claimant, whose claim arose, in part, subsequent to the recording and endorsement of the ship's mortgage therein, contended that, even though a good faith affidavit had been filed, the mortgage could not have been taken in good faith, since no adequate inquiry was made by the mortgagee of the mortgagor concerning the latter's outstanding debts and liens. The court rejected this contention, holding that the failure of the mortgagee to make inquiry as to the financial status of the mortgagor, had no debilitating effect, as there is no stautory duty upon him to do so. The court discussed this, at 271 F. 2d 53, 54, as follows:

> "Since the statute requires an affidavit of good faith by the mortgagor, we may assume that, on proof and finding that the mortgagor and the mortgagee undertook to use the device of a preferred ship mortgage in fraud of creditors, and hence with a design to hinder, delay and defraud any existing or future creditor or any lienor of the vessel, the mortgage would lose its preferred status. But except for such circumstances, *there is no statutory obligation on the part of the mortgagee to make any inquiry.* It might, of course, affect the status of the mortgage as to prior liens—just as perhaps it does here concerning the $1,282.95—but an absence of inquiry does not vitiate the mortgage as such." (Emphasis supplied)

The Special Master, the District Court and the Court of Appeals found (a) that the evidence below abundantly showed that Mastan's mortgage transactions were made in good faith and (b) that such transactions were patently supported by full and complete consideration.

It is conceded by Todd that it rendered its repairs subsequent to the due recordation and endorsement of Mastan's Original Mortgage and the Supplemental Agreement thereto, which secured Mastan's original loan to Sapphire of $1,296,000. As hereinbefore discussed, the Ship Mortgage Act decrees that a lien sounding in tort is a "preferred maritime lien" and, as such, has priority over the lien of a ship mortgage, even if the event giving rise to that lien occurs subsequent to the due recordation and endorsement of the mortgage.

Realizing this, Todd attempted below to convert its repair lien from one based upon contract into one sounding in tort, relying on two cases, to wit, the *Henry W. Breyer*, 17 F. 2d 423 (D. Md. 1927) and *Morrisey et al. v. The SS A & J Faith*, 252 F. Supp. 54 (D. Ohio 1965). Citing these very same cases in the petition, Todd says its lien is one arising from tort because at the time it rendered its repairs to the Sandy, both Sapphire and Mastan knew Sapphire was hopelessly insolvent, that Sapphire had no intention of paying for the repairs and that thus, its repairs were fraudulently accepted. Mastan does not agree with this interpretation of the evidence. Be that as it may, Mastan contends that the cases cited by Todd do not support its position and, further, even if Sapphire was insolvent and did not intend to pay at the time of Todd's repairs, Todd's lien still could not sound in tort.

The suit below was one in admiralty, strictly *in rem*. The issue was the validity and priority of competing maritime lien claims against the Sandy. There was no issue as to *in personam* rights of any of the lien contestants, either between themselves or against Sapphire. It is established beyond peradventure that the test of whether a repairer, such as Todd, has a maritime lien, is whether in rendering his services he relied on the credit of the vessel, as opposed to the credit of the vessel owner. Without reliance on the credit of the vessel, no maritime lien can exist. *In Re Marine Transport*, 94 F. 2d 7 (2 Cir. 1938); *Brock* v. *The SS South Hampton*, 231 F. Supp. 280 (D. Ore. 1964). Thus, insofar as the right of maritime lien of a repairman, such as Todd, is concerned (which is all that was in issue below), the solvency or insolvency of the vessel owner at the time the repairs are ordered and rendered is completely immaterial. What, alone, is relevant, is the solvency of the vessel at the time, i.e. its ability to stand as a credit for the services given. This concept of personification of the vessel, separate from the vessel owner, is reflected in the remedy given to enforce the maritime lien, namely, the suit in admiralty *in rem*. In discussing the nature of the maritime lien and the remedy given to enforce it, 1 *Benedict on Admiralty* §12, at page 22, states:

> "The maritime lien is an appropriation of the ship as security for a debt or claim, such appropriation being made by the law * * * the law creates a remedy for the claim against the ship herself and rests in the creditor a special property in her, which subsists from the moment the debt arises and follows a ship into the hands of an innocent purchaser."

The concept of fraud consists of concealment of a fact from and justifiable reliance on the absence of that fact by the person defrauded. Thus, if a repairer, prior to rendering his services to a vessel, knows that the solvency or credit of the vessel is pledged, in priority, to the lien of another, the repairer cannot later claim that he was defrauded with respect to any lien right his services generated against the vessel since the status of that vessel's credit standing, *which in lien right alone is relevant*, was not concealed from him. It is established that the due recordation and endorsement of a ship mortgage pursuant to the terms of the Ship Mortgage Act gives constructive notice to those who subsequently furnish repairs or services to the encumbered vessel that said vessel is covered by a U.S. preferred mortgage and that the credit of that vessel is pledged first to the lien of that mortgage. Thus, anyone who furnishes repairs or other services to a vessel in the face of the latter is not mislead and does so at his risk. These concepts are reflected in two recent cases which are directly in point, to wit, *Atlantic Steamer Supply Company* v. *The SS Tradewind*, 153 F. Supp. 354 (D. Md. 1957), and *Diaz* v. *The SS Seathunder*, 191 F. Supp. 807 (D. Md. 1961).

Diaz v. *SS Seathunder*, *supra*, involved a lien proceeding against a vessel, the *SS Seathunder*, in which various lien claimants were asserting competing lien rights. One of these lien claimants was a repairer who had rendered repairs to the *SS Seathunder* prior to her arrest. At the time the repairer had rendered said repairs, the *SS Seathunder* was under demise charter (i.e., a type of lease of a vessel in which the vessel owner gives over complete

control and operation of the vessel to the charterer, or leasee). A clause in the charter party covering the vessel provided that the charterer had no authority to pledge the vessel as security for any repairs. Such a clause (a lien prohibition clause) in a demise charter party is the normal practice. The United States Maritime Lien Act (46 USC §§971-975) is to the effect that, if a repairer knows that a vessel is under charter, or should know that a vessel is under charter, he has a duty to investigate whether there is a lien prohibition clause in the charter party. If the repairer does not so investigate and there is such a lien clause, he can have no lien. *Dampskibsselskabet Dannebrog* v. *Signal Oil & Gas Co.*, 310 U.S. 268 (1940). A lien prohibition clause, however, applies only to contract liens and does not apply tort liens against the vessel (*e.g.* liens arising from collision, personal injury) since the latter are deemed created by operation of law.

The repairer realizing he would have no lien because of the lien prohibition clause in the charter party under which the *SS Seathunder* was operating, attempted to convert his contract lien into a tort lien, by using the same argument advanced by Todd below, i.e., that at the time the charterer ordered and accepted the repairs, the charterer was insolvent, unable to pay for same and had no intention of doing so; and that such inability to pay was concealed from the repairer. Thus, said the repairer, his lien was based on tort. To this the court refused to agree.

The court found that the repairer knew of the existence of the demise charter. The court further found that a copy of the charter party containing the lien prohibition clause was on board the vessel at all relevant times.

The statutory duty imposed upon the repairer to investigate, together with the knowledge of the repairer as to the existence of the charter party and the placement of the latter on board the vessel, meant, said the court, that the *SS Seathunder* gave constructive notice to the repairer that her credit (which in maritime lien right is, alone, of concern) could not be pledged to secure payment of the repairs. The court held that the latter had the result that no lien based on fraud could be given to the repairer, as the two vital elements of that fault could not be present, namely:

(a) justifiable reliance by the repairer on the ability of the vessel to stand as security for payment of the repairs, the court stating one "alleging fraud cannot close his eyes to avoid discovery of the truth and still prevail" (191 F. Supp. 807 at 815); and

(b) fraudulent concealment by the vessel of its inability to stand as a credit for payment of the repairs.

An analogous situation was presented in *Atlantic Steamer Supply Co.* v. *The SS Tradewind*, *supra*. This case like the *Diaz* case, involved a competition of lien claims with respect to the sale proceeds of a vessel, the *SS Tradewind*, which had been arrested and thereafter sold. One of the lien claimants ("Smith") was an agent who had been appointed by the vessel owner to render port, cargo and sundry services to the vessel in the port of Havana. Another of the lien claimants was a ship mortgagee whose mortgage had been recorded and endorsed prior to the rendition of Smith's services. Realizing that the prior recording and endorsement of a ship mortgage would mean that his lien would be inferior, Smith attempted to convert

his contract lien into one sounding in tort, alleging the same grounds, as in the *Diaz* case and as Todd below, to wit, that at the time the vessel owner directed him to render services to the *SS Tradewind*, the owner was insolvent, unable to pay and had no intention of paying Smith, all of which was concealed. Indeed, shortly after the services were rendered by Smith, the vessel owner went into voluntary bankruptcy.

Noting that Smith had alleged fraud only against the shipowner and not against the vessel, the court held that this could never give rise to a lien against the vessel citing *International Refugee Organization* v. *Maryland Drydock Co.*, 179 F. 2d 284 (4th Cir. 1950); *Todd Shipyard Corporation* v. *City of Athens*, 83 F. Supp. 67, 76 (D.C. Md. 1949). The court went on to state however, that even assuming fraud was alleged against the vessel, Smith's position would be untenable by reason of the fact that the mortgage was properly recorded and endorsed prior to Smith's rendering of services. Thus said the court:

> "The vessel clearly gave notice, the solvency or insolvency of her corporate owner being irrelevant as to the vessel's representation of her own ability to pay for the services rendered, that her own credit was pledged first to the payment of the preferred mortgage". (153 F. Supp. 354, 358.)

Neither *Morrisey* v. *SS A & J Faith* nor the *Henry W. Breyer* relied on by Todd diminish the above authority or support Todd's position.

The *Morrisey* case involved a lien contest with respect to the sale proceeds of a vessel, *SS A & J Faith*, which had

been arrested and thereafter sold at the behest of a number of lien claimants. One of the lien claimants to the vessel was a preferred ship mortgagee and another was a shipper of cargo. The question was whether the lien of the preferred ship mortgagee or that of the cargo shipper was superior. The shipper had loaded his cargo aboard the *SS A & J Faith* at a time when the vessel owner was floundering on the shoals of hopeless insolvency. The result of the latter was that the vessel never sailed by reason of its being arrested at the port of loading by one of its many lien creditors. The shipper argued that its lien was superior to that of the ship mortgage, as it was founded upon tort. The lien was based on tort, said the shipper, for two reasons:

> (1) the vessel, as a common carrier, had a statutory duty under the *Carriage of Goods by Sea Act* (46 USC §§1300-1315), to be seaworthy and had violated that duty as regard the shipper by reason of the vessel's financial inability to make the voyage;
>
> (2) the act of the vessel owner in accepting prepaid freight, with no expectation of completing the voyage, gave rise to a claim based on fraud.

At common law, a vessel engaged in common carriage, owed an absolute duty to cargo to be seaworthy. The *Carriage of Goods by Sea Act, supra*, modified that duty by the requirement that such vessel need only exercise due diligence to be seaworthy.

While recognizing that the concept of seaworthiness normally meant the physical fitness of a vessel to perform a particular voyage, the court held that the term should not be merely limited thereto but should be extended to include

the financial ability of the vessel to complete the voyage for which it solicits cargo. The court then held that the hopelessly insolvent state existing at the time of loading made the *SS Act of Faith* unseaworthy, and unseaworthy due to lack of due diligence. As this fault was a breach of an extra contractual duty imposed by law, the court held that it sounded in tort. Thus, said the court, was the shipper's lien superior to the lien of the ship mortgage. Having found the latter, the court refused to decide the second ground advanced by the shipper, namely, that the acceptance of prepaid freights by the vessel owner in an insolvent state gave rise to a tort lien based on fraud.

The *Henry W. Breyer* also relied on by Todd is on all fours with the *Morrisey* case i.e., a shipper loading his cargo on board a vessel and prepaying freight only to be met with the failure of the vessel to sail by reason of its arrest by lien creditors. The sole difference between the *Breyer* and the *Morrisey* case is that, at the time the *Breyer* case was decided, the *Carriage of Goods by Sea Act, supra*, had not been enacted and the vessel's duty in regard to seaworthiness was absolute. In any event, the *Breyer* case, like the *Morrisey* case did not give the shipper a tort lien based on fraud but rather held, as is noted in footnote 5 of the *Morrisey* opinion, that the shipper's tort lien was one based on the violation of the common law obligation running to cargo that the carrying vessel be seaworthy.

In *Atlantic Supply Co. v. The SS Tradewind*, the agent "Smith" relied on the *Breyer* case in support of its contention that it had a tort lien based on fraud superior to that of the prior recorded and endorsed ship mortgage. The

court in the latter case made note of the fact that the *Breuer* opinion, itself, showed that it did not support such contention, the court discussing this at 153 F. Supp. pages 361-362.

2. The decision below sustaining the refusal of the Special Master and District Court to apply the doctrine of marshalling of assets does not present an important federal question, as such decision was patently correct, nor does there exist any conflict between that decision and the decision of any other court.

None of the cases cited by Todd in its petition deal with proceedings, as below, to foreclose the lien of a ship mortgage under the Ship Mortgage Act of 1920. These cases then do not support Todd's assertion that the affirmance by the Court of Appeals of the refusal below to apply the doctrine of marshalling of assets against Mastan was a grievous error. Really, the sole support of Todd's assertion in this regard is the plea that equity be done.

While it cannot be denied that equitable considerations have some place in admiralty proceedings, it is submitted that they must be subservient to the substantive and procedural rights conferred by admiralty law, both common and statutory. The proceedings herein are governed *by specific federal enactment*, the Ship Mortgage Act of 1920, which was meant to be comprehensive in and of itself, *Walter E. Heller & Co.* v. *The M/V Mr. Ed, supra; U.S.* v. *American Gas Screw Franz Joseph, supra.* That Act contains nary a mention that funds or collateral extraneous to the foreclosure proceedings be marshalled before the ship mortgagee can realize upon his lien from the proceeds of the sale of the encumbered vessel. If such

a deference to funds or collateral other than the vessel proceeds were intended, it is submitted that the Ship Mortgage Act, which is detailed indeed, would have clearly said so. For example, the Act (46 USC §922(e)) provides that where a ship mortgage covers property other than the vessel, it must provide a separate discharge for such property by the payment of a specified portion of the mortgage indebtedness. It is submitted then that the application of the doctrine of marshalling of assets below could not be sanctioned as a valid exercise of equity, since the same would clearly be in derogation of the contractual lien rights of Mastan, but more importantly would, in effect, amend the Ship Mortgage Act by super-imposing equitable principles not specifically found therein. 4 *Benedict on Admiralty*, §613; *Libel of Pilgrim Trust* v. *The Frances C. Dearborn*, 94 F. Supp. 807 (D. Me. 1950).

Further, any requirement that a ship mortgagee divert his focus from the encumbered vessel or the sale proceeds thereof and cast about to test the worth of other possible collateral would clearly work a dilution of the certainty, and thus value, of the lien of the preferred ship mortgage which, in turn, would violate the very purpose for which the Ship Mortgage Act was created, *i.e.*, the encouragement, stabilization and promotion of the financing of *mortgage security* in ships in the interest of building a strong American Merchant Marine, *Chemical Bank New York Trust Co.* v. *The SS Westhampton*, 231 F. Supp. 284 (D. Md. 1964); *U.S.* v. *American Gas Screw Franz Joseph*, *supra*; *1 Benedict on Admiralty*, §78, p. 181. Thus, did the Third Circuit in its opinion (418 F. 2d 177 (3rd Cir. 1969)) state, at 418 F.2d 180:

> "Moreover there is serious doubt whether marshalling is ever proper where its effect would relegate the preferred mortgage to a status inconsistent with the express priority given it by the statutory direction."

The jurisdiction of the court below is strictly *in rem* over a single fund, i.e. the *Sandy* sale proceeds. The source of that jurisdiction was and is the maritime liens against that fund of the various lien claimants. The court below had and has no power to adjudicate with respect to property to which a maritime lien cannot adhere. As Justice Field wrote in *The Rock Island Bridge*, 73 US (6 Wall) 213, 215 (1867):

> "The lien and the proceedings in rem are, therefore correlative—where one exists, the other can be taken, and not otherwise."

See also *The Resolute*, 168 US 437, 440 (1897); *The Lottawanna*, 88 US 558, 581 (1874); Gilmore & Black, *The Law of Admiralty*, 510 (1957); Robinson, *Admiralty*, p. 362.

As noted in the Third Circuit's opinion, the supposed funds which Todd contends should be marshalled are (1) purported net marine insurance proceeds derived from the *Sandy*, *Gladys* and *Etta* which Todd contends Mastan is entitled to and (2) accounts receivable assigned by Sapphire to Mastan, such accounts primarily consisting of freight, charter hire, etc. purportedly due Sapphire under various contracts of affreightment.

It is well established, however, that marine insurance proceeds are nonmaritime property to which no right of maritime lien can adhere. *Walsh v. Tadlock*, 104 F. 2d 131 (9th Cir. 1939); *The Donald T. Wright*, 30 F. Supp. 610 (W.D. Ken. 1939) and the cases cited therein. A like result

pertains to the accounts receivables (assignments of charter hire, freights). While a vessel is given a maritime lien against cargo to secure the payment of charter hire or freight due on a particular voyage, such lien is strictly possessory and is thus destroyed if the cargo is unloaded, Gilmore and Black, *The Law of Admiralty*, p. 517 (1957). As Sapphire has long since lost its vessels to lien arrests, there is obviously no cargo possessed by it to which liens for freight and hire might attach. Thus any assignments as to the latter, Mastan may have, certainly do not carry any maritime lien rights.

As the marine insurance proceeds and the accounts receivable alluded to by Todd cannot support maritime liens, it is submitted that, under the above law, the court below was and is without jurisdiction to adjudicate a marshalling of same.

The above aside, it is submitted that even if the doctrine of marshalling of assets could in theory be applied below, Mastan would not under the terms of that doctine be required to marshal. This is said for the following:

(a) Said doctrine can apply only if the other fund or property to which the senior lienor, alone, has access, is in the control of or in the hands of a debtor, *common to both such senior lienor and the junior lienor who is seeking the marshalling process*, *Markham* v. *Russel State Bank*, 358 F. 2nd 488 (10th Cir. 1966); *Victor Gruen Associates, Inc.* v. *Glass*, 338 F 2nd 826 (9th Cir. 1964); *In Re Independent Truckers, Inc.*, 226 F. Supp. 440 (D. Neb. 1963); *Gordon* v. *Aratee*, 114 NJ Eq. 294, 168 A. 729. As noted in the Third Circuit's opinion the insurance proceeds on the *Sandy* and the other vessels are in the hand of English underwriters.

While the English underwriters may be considered debtors to Sapphire by reason of the fact that the latter is the named assured under the marine policies on the aforesaid vessels, and while they may be considered debtors to Mastan by reason of the fact that it is loss payee as interest may appear, they are certainly not debtors as to Todd, the latter having no contractual or other relation with said underwriters. A like result must be advanced as regards the accounts receivable, assuming they have any worth at all. While the obligors under these accounts may be considered debtors of Sapphire, by reason of being opposite contractual parties, and debtors of Mastan, by reason of an assignment in its favor, they are certainly not debtors as to Todd, the latter having no contractual or other relation with said obligors.

(b) Said doctrine does not apply where the fund or property as to which the senior lienor, alone, has a right is without the jurisdiction of the court attempting the marshalling. *Lewis* v. *U.S.*, 92 US 618 (1879); *Sowell* v. *Federal Reserve Bank*, 268 US 449 (1925); *Klinger* v. *New York State National Bank*, 151 Misc. 903, 271 N.Y.S. 252; *Sernberger* v. *Sussman*, 69 N.J. Eq. 199, 60 A 195, aff. 85 N.J. Eq. 593, 98 A 1087 (1916). If any insurance proceeds are available to Mastan, they, as noted above, are in the hands of the English underwriters. Thus, they are without the jurisdiction of the court below, the underwriters being obviously in London.

(c) Said doctrine may not be applied where it would compel the senior lienor to engage in litigation, especially where the property or funds as to which marshalling is directed are of doubtful value. *C.T. Willard Co.* v. *City of New York*, 81 Misc. 48, 142 N.Y.S. 11; *Klinger* v. *New*

York State National Bank, supra; *Gordon* v. *Aratee, supra*, or compel him to exhaust a mere personal remedy. 55 CJS *Marshalling of Assets & Securities*, §4."

As discussed above, Mastan has no lien rights as regards the insurance proceeds or accounts receivable alluded to by Todd. Thus, any attempt by Mastan to vindicate a right to said items would not be by *in rem* suit, but by an ordinary *in personam* remedy with all its attendant delay. The value of Mastan's right to the purported insurance proceeds is cloudy. At page 40 of its petition, Todd implies that Mastan has certain legal right to collect the proceeds. The testimony below was just the opposite. The adjuster for the underwriters testified as to the failure of underwriters to pay claims under the *Sandy's* insurance, as to which claims, Todd asserts there is a net due Mastan. This adjuster advised that the funds on these claims were not being sent by the English underwriters because they were aware of Sapphire's bankruptcy and thus, the probable legal problem as how to distribute the funds. Thus, the obvious reality is that Mastan, even if it attempted to vindicate any rights it might have as to the insurance proceeds, could not do so by merely writing a letter, but would have to take the path of litigation, which litigation would most assuredly involve Sapphire's Trustee in Bankruptcy as one of the parties. A like view results with respect to the accounts receivable as to which Todd urges marshalling. As Sapphire is now in bankruptcy, any claim by Mastan to these accounts would involve litigation, which would be complicated by the interest of Sapphire's Trustee in Bankruptcy. Further and most important and as noted in the Third Circuit's opinion, the Special Master found

that the evidence showed the accounts receivable to be worthless.

Characteristic of Todd's straining approach throughout the proceedings below, it asserts on page 39 of its petition, that it is prepared to offer testimony that Mastan assigned to the 046 corporation insurance claims of 130,000 for 15,000. The testimony below showed that this assignment had nothing to do with the mortgage in issue here, was not made for 15,000 and in fact was actually made for Todd's benefit. It is submitted that Todd is guilty of nothing less than a shocking lack of candor to this Court.

(d) Said doctrine may not be applied where it will operate to the senior lienor's prejudice or trench upon his rights; *Victor Gruen Associates* v. *Glass, supra; Philadelphia Home, etc.* v. *Philadelphia Sav. F. Soc.*, 126 N.J. Eq. 104, 8 A 2nd 193; *Gordon* v. *Aratee*, supra; 55 CJS *Marshalling of Assets & Securities*, §4.

It is submitted that application of the doctrine would seriously prejudice Mastan, since it would put Mastan to the vexation of commencing *in personam* litigation with respect to rights of uncertain value in jurisdictions other than the court below, which litigation would be made all the more difficult and which litigation would be prolonged, to say the least, by reason of the competitive right of Sapphire's Trustee in Bankruptcy.

Thus, it is submitted that the Special Master's refusal to apply the doctrine of marshalling of assets, which refusal was sanctioned by both the District Court and the Circuit Court of Appeals was eminently proper on any one of a number of grounds.

II

Mastan respectfully requests that this Court grant it, as against Todd, interest and damages for delay on the ground that Todd's application for writ is totally frivolous.

The judgment below was dated and entered in the District Court for the District of New Jersey on February 17, 1969. In substance, said judgment confirmed the findings of the Special Master that Mastan was entitled to the remaining funds of $55,085.37 in the District Court and directed the Clerk of that Court to pay out of the Registry to Mastan said sum. The enforcement of this judgment for money has been delayed from February 17, 1969 until date, a period of over a year, by reason of Todd's appeal to the Court of Appeals and its present application for certiorari to this Court.

Mastan respectfully submits that the grounds advanced by Todd in its petition are of the most frivolous kind and further were briefed in a manner that simply ignored the clear findings of the Special Master, District Court and Court of Appeals that the evidence below showed that Mastan's mortgage transactions were made in abundant good faith and that same were supported by full and fair consideration. It is respectfully submitted, then, that the present application for writ was prosecuted solely for the purposes of delay. Thus, Mastan respectfully requests that this Court grant it, as against Todd, interest on the sum awarded to Mastan below ($55,085.37) from the date the judgment of the Court of Appeals was entered, to wit, November 18, 1969 until the date the judgment of the District

Court is enforced by payment of the said $55,085.37 to Mastan, the interest rate being at 6% per annum, which is the rate for post-judgment interest allowed by the law of the State of New Jersey, the place where the District Court judgment was rendered and entered. *713 Co. v. Jersey City*, 94 N. J. Super 210 (1967). Mastan further requests that this Court, in addition to interest, exact in its favor, as against Todd, a sum equal to 10% of the sum of $55,085.37 as an award of damages and penalty.

Mastan makes the above application on the basis of Rule 56 of the Supreme Court Rules. *Deming v. Carlisle Packing Co.*, 226 US 102 (1912); *Blair v. Durham*, 139 F. 2d 260 (1943) and the cases cited therein.

Conclusion

For the foregoing reasons it is respectfully submitted that this petition for a writ of certiorari should be denied and that Mastan should be awarded interest and damages as against Todd.

Respectfully submitted,

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